ORAL ARGUMENT HELD APRIL 12, 2016

No. 15-1177
IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

PHH CORPORATION; PHH MORTGAGE CORPORATION; PHH HOME LOANS, LLC; ATRIUM INSURANCE CORPORATION; and ATRIUM REINSURANCE CORPORATION,

Petitioners,

v.

CONSUMER FINANCIAL PROTECTION BUREAU,

Respondent.

ON PETITION FOR REVIEW OF AN ORDER
OF THE BUREAU OF CONSUMER FINANCIAL PROTECTION
(CFPB FILE NO. 2014-CFPB-0002)

RESPONDENT CONSUMER FINANCIAL PROTECTION BUREAU'S PETITION FOR REHEARING EN BANC

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STATEMENT PURSUANT TO FED. R. APP. P. 35(b)

A panel of this Court has rendered a dramatic and unprecedented ruling that purports to override Congress's explicit determination to create "an independent bureau" to exercise regulatory and law enforcement authority in a particular segment of the economy. 12 U.S.C. 5491(a). It thus sets up what may be the most important separation-of-powers case in a generation, since the independent counsel statute was challenged in *Morrison v. Olson*, 487 U.S. 654 (1988).

The panel held that the structure of the Consumer Financial Protection Bureau is unconstitutional because it is headed by a single director who may be removed by the President only for cause. Panel Opinion (Op.) at 10; *see* 12 U.S.C. 5491(c)(3). This decision conflicts with *Humphrey's Executor v. United States*, 295 U.S. 602 (1935), which has long been understood to "bless[] Congress's creation of the so-called 'independent' agencies where at least one individual is appointed by the President to a full-time, fixed-term position with the advice and consent of the Senate and has protection against summary removal by some form of 'for cause' restriction on the President's authority." *Free Enter. Fund v. Public Co. Accounting Oversight Bd.*, 537 F.3d 667, 695 (D.C. Cir. 2008) (Kavanaugh, J., dissenting, internal quotation marks omitted), *rev'd* 561 U.S. 477 (2010). In addition, the decision conflicts with *Morrison v. Olson*, where the Court stated that "we cannot say that the imposition of a 'good cause' standard for removal itself unduly trammels on executive authority." 487 U.S. at 691.

This decision also presents an issue of exceptional importance because it unduly limits Congress's flexibility to respond to "the various crises of human affairs," *McCulloch v. Maryland*, 17 U.S. 316, 415 (1819), by creating independent administrative agencies headed by a single director. And it may affect not only the Bureau but also other agencies headed by a single director removable only for cause (Social Security Administration, 42 U.S.C. 902(a); Federal Housing Finance Agency, 12 U.S.C. 4512(b)(2); Office of Special Counsel, 5 U.S.C. 1211(b)).

In addition, the panel's decision misinterpreted the Real Estate Settlement Procedures Act (RESPA) in a manner that so fundamentally defeats the statutory purpose as to warrant rehearing en banc. The panel held that RESPA permits referrals made in exchange for kickbacks in the form of lucrative mortgage reinsurance business, thus defeating RESPA's statutory prohibition of kickbacks for referrals of real estate settlement service business. To reach that result, the panel overstepped its role in reviewing an administrative decision, ignored key portions of the statutory text, and interpreted the term "bona fide" in a manner inconsistent with Supreme Court precedent. If the ruling stands, it will become easy for lenders and others who make referrals of real estate settlement service business to disguise kickbacks and evade RESPA's prohibition.

STATEMENT OF THE CASE

This case started when the Bureau challenged Respondent PHH Corp.'s kickback scheme as a violation of RESPA. PHH was a mortgage lender, and when some of its borrowers needed mortgage insurance, PHH referred them to independent mortgage insurers. Although borrowers pay the premiums, mortgage insurance protects lenders against the risk of borrower default. Until the collapse of housing prices, the mortgage insurance business was lucrative, and beginning in the mid-1990s, PHH figured out how to tap into those profits. In direct exchange for referrals PHH made to the mortgage insurers (referrals were the only way mortgage insurers got the business), PHH required insurers to pay kickbacks that took the form of premiums for *re*insurance. This reinsurance was a type of insurance the mortgage insurers did not want, but which they purchased from PHH every time PHH sent them a referral because only then would PHH continue sending them referrals. (JA 5-6, 13). Thus, PHH referred borrowers to mortgage insurers that had kickback reinsurance agreements, not those that provided borrowers with the best value.

After an administrative trial, the Bureau held that PHH violated RESPA. (JA 1). RESPA seeks, *inter alia*, to "eliminat[e] … kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services." 12 U.S.C. 2601(b)(2). Section 8(a) provides that, "No person shall give and no person shall accept any fee, kickback, or thing of value pursuant to any agreement or understanding, oral or otherwise, that business incident to or a part of a real estate settlement service involving a federally related mortgage loan shall be referred to any person." 12 U.S.C. 2607(a). The Bureau found that PHH required insurers to purchase its reinsurance as a quid pro quo for its referrals of mortgage insurance business in violation of section 8(a). JA 4, 12-14. The Bureau rejected PHH's argument that section 8(c)(2) of RESPA excused its violations. That section permits "the payment to any person of a bona fide salary or compensation or other payment for goods or facilities actually furnished or for services actually performed." 12 U.S.C. 2607(c)(2). The Bureau held that, even if PHH charged fair market value for the reinsurance, the payments were "a thing of value" because they enabled PHH to sell profitable reinsurance. And the payments were not "bona fide compensation … for services" because they were a quid pro quo for referrals. JA 12-13, 18-20. The Bureau also noted that PHH's interpretation of section 8(c)(2) would render section 8(b) meaningless and sections 8(c)(1)(B) and (C) surplusage.[1] JA 19. The Bureau imposed injunctive relief barring PHH from accepting kickbacks and ordered disgorgement of the kickback payments it had received since 2008, a total of $109 million. JA 39-40.

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[1] The Bureau also held that, even if it accepted PHH's interpretation of section 8(c)(2), it would still have concluded that PHH violated RESPA. JA 20-22.

PHH sought review and a panel of this Court reversed. First, the panel concluded that "the CFPB is unconstitutionally structured because it is an independent agency headed by a single Director." Op. at 64. According to the panel, "independent agencies are unaccountable to the President and pose a greater threat to individual liberty because they operate free of the President's supervision and direction," *id.* at 55, regardless of whether the agency is "headed by one, three, or five members," *id.* at 56-57. The panel distinguished *Humphrey's Executor*, *supra*, which upheld the constitutionality of the Federal Trade Commission, based on its view that the Bureau is "a historical anomaly." Op. at 27. According to the panel, the multi-member structure at other agencies "reflects a deep and abiding concern for safeguarding the individual liberty protected by the Constitution," *id.* at 43, and "acts as a critical substitute check … to prevent arbitrary decisionmaking and thereby to protect individual liberty," *id.* at 9. Relying on its preference for the multi-member structure, the panel majority concluded that the Bureau's structure "poses a constitutional problem even if it does not occasion any additional diminishment of Presidential power beyond the significant diminishment already caused by *Humphrey's Executor*." *Id.* at 59. As a remedy, the panel severed the for-cause removal provision from the Bureau's enabling act. *Id.* at 69.

Next, the panel reversed the Bureau on PHH's RESPA violations. It recognized that section 8(a) prohibits kickbacks for referrals, *id*. at 73, but held that, taken together, sections 8(a) and 8(c)(2) unambiguously permit "tying" a referral to a purchase, and that payment for the tied service is bona fide as long as it is for reasonable market value, *id*. at 74. The panel held that the Bureau's interpretation of those sections was contrary to HUD's "longstanding interpretation," *id.* at 75, and that even if the Bureau's interpretation were correct, it would violate due process to apply that interpretation retroactively to PHH, *id.* at 83. Accordingly, the panel remanded the matter to the Bureau for further proceedings consistent with its interpretation of RESPA. *Id.* at 100-101.

Judge Randolph concurred and opined that the administrative law judge who presided over the Bureau's trial was an inferior officer not appointed in conformity with the Appointments Clause. Judge Henderson dissented because she would have declined to reach the constitutional issue under the rule of constitutional avoidance.

ARGUMENT

I. THE PANEL'S DECISION CONFLICTS WITH *HUMPHREY'S EXECUTOR v. UNITED STATES* AND *MORRISON v. OLSON*

The panel would sever section 1011(c)(3), 12 U.S.C. 5491(c)(3), from the Consumer Financial Protection Act, 12 U.S.C. 5481, *et seq.* (CFPA). That provision makes the Bureau's director removable by the President only for cause. But the panel's reasoning about the constitutional basis for removing the director is at odds with Supreme Court precedent. In *Humphrey's Executor*, a case involving the Federal Trade Commission (FTC), the Court held that Congress can "create independent agencies run by principal officers appointed by the President, whom the President may not remove at will but only for good cause." *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 483 (2010). In *Morrison v. Olson*, the Court explained that *Humphrey's Executor* "found it 'plain' that the Constitution did not give the President 'illimitable power of removal' over officers of independent agencies." 487 U.S. at 687 (quoting *Humphrey's Executor*, 295 U.S. at 629). According to the Court, "the real question is whether the removal restrictions are of such a nature that they impede the President's ability to perform his constitutional duty." *Morrison*, 487 U.S. at 691.

The panel addressed "the real question" posed in *Morrison*. It held that, because of for-cause removal, "independent agencies are unaccountable to the President," regardless of whether the agency is headed "by one, three, or five members." Op. at 55, 56. The panel found it problematic that "[t]he independent status of an independent agency erects a high barrier between the President and the independent agency regardless of how many people head the independent agency on the other side of the barrier." *Id.* at 57. But that position is directly at odds with the Court's holding in *Morrison* that, "[c]onsidering for the moment the 'good cause' provision in isolation … we cannot say that the imposition of a 'good cause' standard for removal by itself unduly trammels on executive authority." 487 U.S. at 691. The Court explained that as long as the official "may be terminated for 'good cause,' the Executive … retains ample authority to assure that the [official] is competently performing his or her statutory responsibilities." *Id.* at 692. Thus, for-cause removal does not "interfere impermissibly with [the President's] constitutional obligation to ensure the faithful execution of the laws." *Id.* at 693.

The panel also said that the Bureau's structure "depart[s] from history." Op. at 58. It referred to the Bureau as "the first of its kind and a historical anomaly." *Id.* at 27. Although it recognized that three other agencies are also headed by a single person removable for cause, it wrote them all off because none "has deep historical roots." *Id.* at 29. But the "historical roots" of the FTC were not very deep when the Court upheld its structure in *Humphrey's Executor*, and the few other independent agencies that existed at that time (*e.g.*, Interstate Commerce Commission, Federal Reserve Board) could also have been considered historical anomalies. Further, in *Morrison*, the Court upheld the for-cause removal provision that applied to the independent counsel without any reference to a historical antecedent. 487 U.S. at 685-93. As the Court has recognized, "[o]ur constitutional principles of separated powers are not violated, however, by mere anomaly or innovation." *Mistretta v. United States*, 488 U.S. 361, 385 (1989). The Bureau performs functions similar to the FTC.[2] Although it is headed by one director instead of five commissioners, this does not render the CFPA's for-cause removal provision unconstitutional.

The underlying premise of the panel's opinion is that, regardless of the number of individuals who head an agency, for-cause removal renders the agency "unaccountable to the President." Op. at 55-56. So how did the panel conclude that an agency headed by a multi-member commission will nonetheless pass constitutional muster, whereas one headed by a single director will not? The panel's answer had nothing to do with a lack of presidential accountability. The panel opined that "multi-member commissions or boards … reflect[] a deep and abiding concern for safeguarding the individual liberty protected by the Constitution." *Id.* at 43. The panel thus rested its ruling on criteria that lack definition or boundary and have no foundation in Supreme Court precedent or separation-of-powers principles. *See id.* at 44-47. The panel also found it to be a benefit that, with a multi-member agency, "no single … member possesses authority to do much of anything." *Id.* at 44. Again, this presumed benefit has nothing to do with presidential accountability. The panel claimed that "[t]he check from other commissioners or board members *substitutes* for the check by the President." *Id.* at 53 (emphasis added). But even if fellow commissioners can keep

[2] The scope and nature of the Bureau's authority do not distinguish it from the authority possessed by the FTC at the time of *Humphrey's Executor*. *Compare* 12 U.S.C. 5511(c) (statement of the Bureau's functions) *with* 15 U.S.C. 45, 46(a), 46(d), 46(g) (1934) (FTC's functions).

an eye on one another, they cannot remove one another. The panel thus failed to draw a meaningful constitutional distinction between a multi-member commission and a single-director agency, or to explain how Article II even allows for such a substitute check – the President either has sufficient authority or he does not. *Morrison* holds that, even if an official may be removed only for cause, the President "retains ample authority to assure that the [official] is competently performing his or her statutory responsibilities," 487 U.S. at 692, and this remains true regardless of how Congress has decided, within the scope of its proper constitutional authority, to establish and structure the leadership of an independent administrative agency.

Finally, the panel ignored several features of a single-member agency that make it *more* accountable to the President. A multi-member structure may impede the President's ability to hold any particular official responsible for the agency's performance. "Without a clear and effective chain of command, the public cannot 'determine on whom the blame or the punishment of a pernicious measure, or series of pernicious measures ought really to fall.'" *Free Enterprise*, 561 U.S. at 497 (quoting The Federalist No. 70, p. 476 (J. Cooke ed. 1961)). And though the panel was concerned that "[a] President may be stuck for his or her entire four-year term with a single director appointed by a prior President," Op. at 58, similar situations could arise with multi-member agencies. Because the five FTC commissioners serve staggered terms of seven years (and did so also at the time of *Humphrey's Executor*), the President often could be unable to nominate a majority of commissioners during a term in office. However, because the Bureau's director serves a five-year term, the President will usually be able to select a director of his or her choosing, even in a single term of office.

The panel's holding – that for-cause removal is unconstitutional as applied to the Bureau's director – conflicts with both *Humphrey's Executor* and *Morrison*. That decision should be reconsidered by the Court sitting en banc.

II. THE PANEL'S INTERPRETATION OF RESPA WOULD DEFEAT A PRIMARY PURPOSE OF THAT ACT

For many consumers, real estate transactions are the largest and most complex transactions in their lifetimes. To complete the transaction, consumers typically contract with a real estate agent, a mortgage lender, a title insurance company, a settlement agent, and perhaps others. Often consumers are referred from one provider to the next without exercising much conscious choice.

Congress enacted RESPA because it found that "significant reforms" were needed to "insure that consumers … are protected from unnecessarily high settlement charges caused by certain abusive practices." 12 U.S.C. 2601(a). A primary purpose of the statute is to "eliminate kickback or referral fees that tend to increase unnecessarily the cost of certain settlement services." *Id.* 2601(b)(2). Section 8(a) of RESPA achieves that end by expressly prohibiting "any fee, kickback, or thing of value" that is tied to the referral of "real estate settlement service" business. *Id.* 2607(a). Section 8(c)(2) clarifies that the prohibition does not interdict "bona fide" compensation for goods "actually provided" or for services "actually performed." *Id.* 2607(c)(2). But the panel interpreted section 8(c)(2) to allow the very kickbacks that section 8(a) prohibits, as long as the kickbacks are disguised as a purchase of goods or services. Op. at 73. The panel reached this result through two errors of statutory construction with major import, then compounded its errors by mistakenly holding that the Bureau's interpretation of RESPA violates PHH's due process rights.

1. First, the panel erroneously read the phrase "thing of value" entirely out of the statute, never even mentioning it and stating instead that "Section 8(a) proscribes payments for referrals. Period. It does not proscribe other transactions between the lender and mortgage insurer." Op. at 74. The panel so held despite the fact that PHH specifically tied referrals of mortgage insurance business to required payments in the form of reinsurance premiums. See JA 4-5 (discussing the direct link between PHH's referrals and the mortgage insurers' purchase of reinsurance). PHH thus made referrals based upon its own economic interest rather than the best interest of the consumer. In exchange for these referrals it received profitable kickbacks from mortgage insurers who purchased reinsurance. This is certainly "a thing of value." *See* 12 C.F.R. 1024.14(d) (broadly defining "thing of value"). The

panel's reading of the statute would permit any mortgage lender to condition referrals on the purchase of goods or services in any related or unrelated business line. Such schemes flout the core purposes of RESPA.

Second, the panel erred by interpreting the term "bona fide" in a nugatory manner that conflicts with decisions of the Supreme Court and this Court that have construed the same term in other statutes. The panel held that a payment is "bona fide" whenever it is made for goods or services priced at fair market value, even if the payor had no desire to purchase the goods or services and did so only as a condition of receiving referrals. Op. at 47-75. But how could a payment be "bona fide" – which literally translates as "in good faith" – when it is made for the purpose of procuring referrals and thereby evading an essential provision of a statute? As the Supreme Court and this Court have held when interpreting other statutory provisions, bona fide "suggests absence of evasion." *McDonald v. Thompson*, 305 U.S. 263, 266 (1938) (construing the Motor Carriers Act of 1935); *see also Svalberg v. SEC*, 876 F.2d 181, 183 (D.C. Cir. 1989) (construing NASD rules). Here, the mortgage insurers purchased reinsurance from PHH as a condition of obtaining referrals, thereby providing PHH with a means of profiting from those referrals.

The panel's decision divorced "bona fide" from its roots, and thus would undermine enforcement of section 8(a) by making evasion easy. Indeed, any party making referrals could buy a product at wholesale and then require the party receiving referrals to purchase some of the product at retail every time it received a referral, even if the purchaser had no use for the product. This arrangement could be quite profitable for the party making referrals, yet the panel would authorize it so long as the party receiving referrals bought the product at a fair market price. But this understanding of the statute would allow parties to give or accept a "thing of value" in return for referrals of business, thus defeating the core aim of Section 8(a). This result would have serious detrimental effects on the ability of public officials and private litigants to enforce RESPA and police the giving or receiving of kickbacks in exchange for referrals of business, which the law plainly prohibits.

2. The panel also held that, even if the Bureau's interpretation of RESPA were correct, it could not be applied retrospectively in this case because it represented "a complete about-face from the Federal Government's longstanding prior interpretation of Section 8." Op. at 79. This holding conflicts with *Clark-Cowlitz Joint Operating Agency v. FERC*, 826 F.2d 1074 (D.C. Cir. 1987) (en banc), where this Court held that in an administrative proceeding, an agency could reverse a prior interpretation and apply the new interpretation to the case at hand unless there is a "severe impact and justifiable reliance on contrary agency pronouncements." *Id.* at 1081. Although the panel's refusal to permit the Bureau to apply its interpretation retrospectively is perhaps not worthy of en banc review on

its own, this holding may have been based on the panel's misinterpretation of section 8 of RESPA. Accordingly, if the Court reviews the panel's interpretation of RESPA, we ask for an opportunity to address this holding also.[3]

CONCLUSION

For the foregoing reasons, this Court should grant rehearing.

Respectfully submitted,

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[3] The panel incorrectly claims that PHH acted in "justifiable reliance" on an unpublished 1997 HUD informal staff opinion letter. Op. at 80, 86. But PHH did not justifiably rely on the letter because, according to HUD regulations, that letter was "unofficial," did not express the views of the HUD Secretary, and provided no defense to RESPA liability. 24 C.F.R. 3500.4(b) (1997). In addition, the letter was internally inconsistent. *See* JA 18. The panel also referred to a provision of RESPA regulations. 24 C.F.R. 3500.14(e) (1977); *see* Op. at 81. But that provision had been removed from HUD's regulations by 1995, when PHH commenced its kickback arrangement.